

BRITISH AIRWAYS' £100 MILLION DISPUTE?



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March 2010

British Airways' cabin crew are about to start the second period of strike action in the course of the current dispute. This will run for four days from March 27-30.

This is a serious dispute which Unite did not seek at a major British company. We believe it has already done considerable financial and reputational damage to BA, far in excess of what the company has itself admitted.

Earlier this week, the BA press office sent out a remarkable email to journalists covering the dispute. In effect, it warned them to take all the figures offered by the company – on flights, numbers of crew working, passengers carried, and financial losses – as gospel, and to not report any counter figures offered by cabin crew or their union.

This scandalous attempt at censorship was founded on the argument that, since BA is a public limited company, it is legally obliged to tell the truth and not to mislead the markets.

Doubtless so. However, BA is also obliged not to enter price-fixing rackets. But it did, and has been heavily fined for doing so.

And BA is also obliged not to wage a "dirty tricks" campaign against competitors. But this has happened too, although neither occurred under the present management.

So can we take management's word for it that the losses BA has sustained in the present dispute amount to no more than £7 million per day of strike action? If it is indeed the truth, we believe it is not the whole truth and nothing but.

Certainly, BA has a motive for trying to put the best "gloss" possible on its situation. Unite believes that the company has embarked on an ambitious and expensive attempt to destroy trade unionism among its cabin crew, and that it needs to keep the investment community on side at all costs to see this campaign through.

Some may perhaps see this as a price worth paying if trade unionism is fatally weakened in part of BA's operations. But at any price? And is this damage compatible with the survival of the British Airways brand as it is presently seen?

Unite believes that these are questions shareholders and investors should be asking of British Airways' board. So here we seek to present an alternative analysis of the costs incurred. Of course, we do not pretend to have access to all the information which BA management holds. But all the figures we cite come from reliable sources, who cannot be identified for obvious reasons. Where we are making the best-informed guess we can, we indicate that. Unite has no desire to "mirror" BA's distortions with our own.

HAS THE STRIKE COST BA JUST £7 MILLION A DAY?

On Tuesday March 23, BA issued a statement saying that each day of strike action had cost the company £7 million pounds, making a total to date of £21 million.

Privately, BA has allegedly mentioned different – higher – figures. On Thursday March 18, media were reporting that Willie Walsh had put the figure at £27 million in lost bookings alone. BA did not deny this figure when approached by journalists.

An analysis from Citigroup puts the total cost at around £17 million per day, while a revised analysis from JP Morgan went for a range of £15-20 million per day, a figure which they had reduced from a higher amount once the company announced the extent of its "contingency arrangements." Bloomberg also cited an analyst on 24 March as putting the cost of seven days of strike action as £105 million, or £15 million per day.

None of these figures are exact, of course. But they all point to a much higher sum than the £7 million asserted by BA.

Total losses sustained by the company are made up of several different elements.

LOST PASSENGER REVENUE

The company admits that it cancelled more than half its scheduled flights over the first three-day strike, but claims that it still carried 65 per cent of its passengers. So 35% of its booked passengers would have been expected to receive a refund.

According to JP Morgan Cazenove, BA's average daily passenger revenue is £20 million, not allowing for seasonal fluctuations. So it is plausible that around one-third of this - £7 million or so – has been lost for each day of the strike. Perhaps it is this which BA was referring to in its announcement of March 23. But that lost revenue is far from being the whole picture.

Of the 65% of passengers BA claims to have carried, many were booked onto other carriers, which retained the revenue themselves. Competitors like Virgin and Lufthansa, which could of course keep many of these passengers as long-term customers, will be the beneficiaries. JP Morgan Cazenove estimates that the cost of re-booking passengers on other flights at short notice amounts to around 20% of average daily revenues, or around £4 million.

AEROPLANE HIRE

Because this is a dispute directed at breaking trade unionism, BA has invested heavily in strike-breaking measures which would otherwise make little business sense. An example is the cost of "wet lease" aeroplane hire – that is, planes which come fully crewed.

A well-connected source has told Unite that on one contract alone, the hire of twenty planes for the three-days strike last weekend came to £7 million. All together, we believe BA used around 40 "wet-lease" planes, which would mean on this head alone, BA probably spent

around £14 million over the three days.

During the second strike, this bill may rise even further. The CEO of Ryanair, Michael O’Leary, has told the *Daily Telegraph* (March 23) that he leased three planes to BA over the first strike, but will lease “four or five” for the second strike. The bill for this will also obviously rise.

HOW MANY FLIGHTS DID BA FLY?

The foregoing calculations take at face value BA’s own estimates for the number of flights it flew during the three-day strike, and the number of passengers it carried, as a result of its “contingency plan”.

In fact, we believe that these estimates are themselves flawed. For example, on Sunday March 21, BA aimed to operate 78 flights on its contingency schedule, but in fact flew just 63, cancelling 15 because (in most cases) of insufficient crew. Of the 63 which did fly, 37 carried passengers, but significantly below capacity (some with as little as 14% load).

On Monday March 22, BA again cut planned Worldwide flights – more severely, we believe, than on the previous day. 18 scheduled long-haul flights were cargo-only, something BA does not usually do, because a cargo-only flight does not need cabin crew. In total 37 flights ran “empty”, with no passengers on board, in the hope that they could be crewed from another destination later in the day.

BA have of course offered higher figures for number of flights and for number of passengers carried. Without being in themselves untrue, Unite believes that they include large numbers of both planes and passengers on inbound flights arriving in the UK over the strike days. These flights would not under any circumstances have been affected by the strike call.

We cannot quantify the losses over and above those accounted for previously, but it is our view that they are likely to be significant.

HOW MANY CREW BROKE THE STRIKE?

This is a crucial question at two levels. First, it indicates the strength of support for the strike and the likelihood of its successful maintenance. Second, without crew, BA cannot have been flying passenger aeroplanes.

First, BA claims to have secured 1,000 volunteers from elsewhere in the company to work as cabin crew during the strike. Unite understands that in fact only 350 such volunteers actually flew last weekend. Two-thirds of those who volunteered to train as crew did not pass the basic safety training required before crew are allowed to fly.

Many of the strike-breaking crew used by the company were pilots, who require considerably less training. Many of the flights on Monday March 22 for example were crewed in the cabin by four pilots, two managers and only two regular cabin crew, the total of eight meeting the minimum permissible complement under Civil Aviation Authority regulations.

Our information is that seventy-five per cent of crew supported the

strike call at the weekend. The higher figures published by BA include crew flying into Heathrow on inbound flights from elsewhere in the world – such crew were not expected to take strike action which would have left them marooned far from home.

FURTHER COSTS

The company will sustain further losses not directly attributable to a “strike day” and therefore not included in BA’s own figures. A strike of this nature unavoidably has knock-on effects leading to cancellations and other disruption in the days following a strike. This will add considerably to BA’s lost revenue.

Again, we cannot responsibly put a figure on these “post-strike” losses, but they will likely be considerable.

TOTAL COST

From all the foregoing, it would seem that the analysts’ estimates of a daily loss of £15-20 million may be correct. If you add together the cost of lost bookings, of revenue effectively transferred to other airlines along with BA passengers, the cost of “wet-leased” aircraft and the cost of knock-on “post-strike” disruption, this is the ball-park area we are in.

Over three days of strikes we could then conservatively estimate the total cost as around £45 million. Over seven days of strikes, this dispute will therefore have cost British Airways over £100 million.

That is even before adding on the imponderable cost of missed bookings because of uncertainty over the reliability of future operations.

This is a staggering amount to be spent on an avoidable dispute. It begs the obvious question:

WHY IS BA SPENDING SO MUCH?

It would seem clear that BA have spent vastly more attempting to break the strike than they could have spent on resolving it.

It is not disputed that, in the current economic environment, the company needed to make savings. That is why cabin crew volunteered, after negotiation, a comprehensive programme of cost reductions aimed at meeting management’s requirements. Unite believes these concessions amounted to £62 million, the target set by management. BA dispute this, and assert they amounted to only £52 million.

The difference was therefore £10 million, a gulf that could and should have been bridged before a dispute costing much more became inevitable.

BA’s strategic aim was to incrementally embed a lower-cost “new fleet” of cabin crew in its operation. Unite agreed that this could proceed, seeking only guarantees regarding the pay and conditions of its existing membership.

In this situation, BA has twice made offers to settle the dispute, only to withdraw them the very next day before the union had any opportunity to discharge its democratic obligation to consult its members.

This is not the conduct of a management which wishes to maintain peaceful industrial relations. It only makes sense in the context of trying to deunionise its cabin crew, and to use that advantage to reduce cabin crew rates of pay and other conditions towards those prevailing in budget airlines, over time.

CABIN CREW PAY

This has been justified by reference to the allegedly high rates of pay enjoyed by cabin crew. Unite makes no apology for seeking and securing better pay for its members than would be paid in non-union or weakly-unionised airlines.

However, the pay rates quoted for BA cabin crew in the media are grossly misleading. Basic pay is £12,000 per year, which is increased via a variety of allowances to an average pay level of £22,000 per year, similar to rates at Virgin Atlantic. Increments can raise this figure further, but very few staff earn anything like the £50,000 peak quoted by BA in the media. This could only refer to a tiny minority who have reached managerial level and have thirty or more years' experience.

Unite's contention is that these rates – which we offered to reduce in negotiations with the company - cannot be considered excessive when it is borne in mind that British Airways is a premium airline which trades heavily on the quality of the in-flight service provided by cabin crew.

BRAND DAMAGE

BA depends on high-paying premium and business passengers to make a profit. These passengers expect high-quality service from skilled, professional and friendly cabin crew.

BA has been cutting back on food and other amenities on board. Sometimes, first-class customers may get only their third-choice meal, and crew also report frequent shortages of things ranging from cutlery to duvets.

It is Unite's contention that reducing crew complement on flights – the issue at the heart of this dispute – can only make things worse. Having cabin crew divided by the hostility which frequently accompanies such strikes will not help with the on-board atmosphere either. BA has already fallen from being one of the top businesses to work for in surveys in the 1990s to ranking nowhere in such lists today.

Management's strategy has therefore exposed the company to significant competitive risk, with market share shrinking as premium passengers switch to other airlines. Both Virgin Atlantic and BMI are

reporting increased bookings because of the strike. Will these customers come back if the dispute is prolonged?

This strike follows other problems at BA which have nothing to do with cabin crew or other Unite members at the company – the bungled launch of Terminal Five, the price-fixing and cargo cartel fines included. While the recession has surely been the main factor in generating two years of record losses at BA, management cannot pretend it is all nothing to do with them.

There is only so much self-inflicted trashing a brand can take. Many analysts understand this. Already some are saying a strike poses a "competitive risk" for BA and will hurt the carrier's market share as customers switch to other airlines.

Oddo Securities (24 March 2010) has placed a "reduce" rating on the stock and the influential 7 Investment Management in London, which holds BA shares, said the dispute is still a "negative" for BA, suggesting talks will be needed before this view can change (24 March 2010).

THE WAY FORWARD

The investment community has a part to play in bringing about the outcome we all desire – a negotiated settlement that addresses staff concerns about crew complements, pay and the impact on them of "new fleet", while giving the company the efficiencies and economies it needs.

Unite negotiates similar agreements with thousands of companies and organisations across the economy – private sector and public, from finance to manufacturing – every year. But it goes without saying that we can never negotiate the destruction of free trade unionism anywhere.

BA's future can only be described as unstable. That is bad news for the hundreds of thousands who depend on it for a living, directly or indirectly. It is also bad news for investors used to treating BA as a blue-chip stock.

Shareholders must ask themselves – is management strategy the right one for the airline's long-term prospects and prosperity? The problem was put in a nutshell by a commentator on the PPRune specialist website for pilots and crew this month:

"BA shareholders should be jumping up and down. This is a no-win strategy for Walsh. If he wins he will have grumpy, disillusioned crew and unhappy customers. If he loses, and especially if it takes time to get rid of him, then the airline's shareholders will wear substantial losses, and BA will still have grumpy, disillusioned crew."

That is a future worth avoiding. A sensible, negotiated agreement will be money in the bank for shareholders, and will keep a world-famous brand airborne.

That is the strategy Unite commends